**Before the**
**FEDERAL COMMUNICATIONS COMMISSION**
**Washington, D.C. 20554**

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| In the Matter of | ) | |
| | ) | |
| International Settlements Policy Reform | ) | IB Docket No. 02-324 |
| International Settlement Rates | ) | IB Docket No. 96-261 |
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## *REPLY COMMENTS OF KDDI CORPORATION*

KDDI Corporation ("KDDI") hereby submits these brief reply comments regarding the *Notice of Proposed Rulemaking* ("*NPRM*") issued by the Federal Communications Commission ("FCC") in the above-captioned proceeding on October 11, 2002. *In the Matter of International Settlements Policy Reform and International Settlement Rates*, IB Docket Nos. 02-324 & 96-261, FCC 02-285, rel. Oct. 11, 2002 ("*NPRM*"). The FCC extended the deadline for submitting reply comments to February 18, 2003. *Public Notice*, DA 03-212, released Jan. 28, 2003.

KDDI is the largest facilities-based (Type I) international carrier in Japan, and KDDI also is a competitive provider of mobile services in Japan. In these reply comments, KDDI shall address the FCC's settlement rate benchmark policy as well as the issue of foreign mobile termination rates.

### *I. THE FCC SHOULD REMOVE ITS BENCHMARK POLICY*

The FCC's current benchmark policy works by strictly controlling the settlement payments that U.S. international carriers are permitted to make, thereby forcing foreign telecommunications carriers to accept FCC-prescribed benchmark rates. From the inception of this policy in 1997, there has been a potential conflict with any foreign Government or regulatory agency that sought to regulate the settlement rates charged by its own carriers. The possibility of a direct conflict of laws was recognized by the U.S. Court of Appeals for the District of Columbia Circuit when it upheld the FCC's benchmark policy in *Cable & Wireless plc. v. FCC*, 166 F.3d 1224, 1230 (D.C. Cir. 1999). The Court declined to decide whether the FCC has authority to adopt and enforce its benchmark policy in a conflict-of-laws situation, but upheld the FCC's policy because no such conflict appeared to exist at that time. Hence, it remains an open legal question in the U.S. whether the FCC has sufficient statutory authority to implement its benchmark regime against the contrary wishes of a foreign jurisdiction.

As a practical matter, the benchmark policy works only in cases where the foreign Government or regulatory agency does not intervene to mandate a different or inconsistent result. The benchmark policy is a unilateral FCC policy which is inherently incapable of reconciling issues created by another jurisdiction's adoption or enforcement of its own unilateral policy. In this proceeding, several parties have noted recent developments whereby some foreign jurisdictions have sought to increase the current termination rates up to the level of a specified mandatory floor. In KDDI's views, such unilateral actions cannot be satisfactorily addressed by a more vigorous use of the FCC's own unilateral benchmark policy, but instead require bilateral or multilateral dispute resolution through the ITU or WTO.

In KDDI's view, the appropriate solution is for the United States and other countries to move away from unilateral policies governing termination rates for international switched telephony. There are many other forces at work to ensure reasonable termination rates. KDDI would note that the settlement rates in effect between KDDI and U.S. international carriers were already below the benchmark level when the FCC first adopted its benchmark policy in 1997. Those rates have been consistently reduced since 1997 through a series of commercial negotiations between KDDI and U.S. international carriers. KDDI's experience demonstrates that the FCC's benchmark policy is not necessary to ensure reasonable termination rates for international switched traffic.

In addition, KDDI has concerns about the efficacy of the FCC's benchmark classification system. The FCC created four different categories of countries based upon data regarding per capita gross national product, and a fifth country category is based upon teledensity. This classification system has always had no more than a tenuous connection to the country-specific conditions that affect international termination rates.

In sum, KDDI believes that the FCC should remove its settlement rate benchmark policy.

## *II. THE FCC SHOULD NOT TAKE UNILATERAL ACTION ON THE ISSUE OF FOREIGN MOBILE TERMINATION RATES, BUT RATHER SHOULD ADDRESS THE EXCESSIVE PROFIT MARGINS EARNED BY U.S. CARRIERS*

In the *NPRM* (at ¶51), the FCC sought comment on whether foreign mobile termination rates "are detrimentally affecting U.S. consumers and competition in the U.S.-international services market." The FCC noted (at ¶¶ 45-46) that U.S. international carriers are imposing rate surcharges on U.S. consumers in order to recoup additional costs for terminating traffic to foreign mobile networks. In some cases, the surcharges are higher than or close to the applicable benchmark rate on the route. The FCC also asked parties (at ¶ 51) to comment on whether and how the FCC could effectively address this issue through new policies or regulations, or whether the FCC should rely in the first instance on educational efforts and market forces.

KDDI submits that the issue of foreign mobile termination rates is not suitable for unilateral intervention by the FCC. The termination rates charged by foreign carriers for use of foreign fixed or mobile networks is properly the jurisdiction of the foreign National Regulatory Authority ("NRA"). With respect to mobile termination rates, the level of the rate normally will vary depending upon whether the country adheres to the Receiving Party Pays ("RPP") regime or the Calling Party Pays ("CPP) regime. In general, there is a trade-off between retail subscriber rates and carrier-to-carrier termination rates under these regimes -- the RPP regime results in higher retail subscriber rates and lower (or zero) termination rates, while the CPP regime results in lower retail subscriber rates and higher termination rates.

In KDDI's view, the decision whether to adopt the RPP or CPP regime is one for each country to make based upon its own circumstances and public policy objectives. It is not appropriate for the NRA in a country with the RPP regime to seek to determine or review the level of the mobile termination rates in a country with the CPP regime. (Nor would it be appropriate for an NRA in a country with the CPP regime to seek to determine or review the level of retail mobile rates in a country with the RPP regime.) It is the responsibility of each NRA to review the termination and retail rates charged by mobile operators in its country, and to take the actions, if any, that are necessary to ensure adequate rates.

Further, the FCC should not seek to judge mobile termination rates by comparing them to the rates charged to terminate traffic on fixed networks. It is the experience in Japan and many other countries that the costs of building and operating a mobile network are higher than the costs pertaining to fixed networks. Therefore, it is appropriate that calls to foreign mobile networks should pay a higher termination fee than calls to foreign fixed networks, and it is the responsibility of the NRA in that country to make sure that the rates are adequate.

The issue of mobile termination rates in foreign countries is different than the situation faced by the FCC with respect to high settlement rates in the mid-1990s. International settlement rates applied solely to incoming international calls, and as a result foreign regulators often did not actively regulate those charges. By contrast, many foreign NRAs are actively examining the issue of mobile termination rates, which normally are the same for both domestic and international calls. Therefore, there is less need for direct FCC intervention with foreign mobile termination rates than with international settlement rates.

KDDI submits that the problem of foreign mobile termination rates identified by the FCC in the *NPRM* has been substantially exacerbated by the pricing practices of U.S. international carriers. When U.S. consumers place international calls to mobile telephones in Japan, they are required to pay the normal retail charge for the call as well as a "mobile surcharge." The mobile surcharge for calls to Japan is $.19/minute for most U.S. international carriers. (One of the major U.S. carriers reduced its surcharge to $.14/minute just after the FCC commenced this proceeding.) While these surcharges are lower than the surcharges imposed on calls to some other countries, they nevertheless embody a certain profit margin for the U.S. carriers because they are significantly in excess of the underlying mobile termination costs that the U.S. carriers actually incur on the U.S.-Japan route.

In accordance with ITU-T Recommendation D.93, U.S. international carriers have been negotiating a separate bilateral settlement rate with KDDI and other foreign carriers for traffic terminating on a mobile network. Initially, the difference between the international termination rate for non-mobile and mobile terminating calls was approximately $.19/minute on the U.S.-Japan route. Since that time, the international termination rates for both non-mobile and mobile terminating calls for Japan have been reduced on a regular basis in light of relevant cost and market trends. To date, the difference between the termination rate for non-mobile and mobile terminating traffic (based on weighted average rates) has been reduced by approximately 30%. Nevertheless, the major U.S. international carriers have not passed through these cost reductions to their subscribers. While one U.S. carrier recently revised its surcharge, other U.S. carriers continue to impose a surcharge of $.19/minute on the U.S.-Japan route, and those U.S. carriers are earning a 42% positive margin solely on the mobile termination surcharges they impose on their U.S. subscribers.

The FCC should address the excessive profit margins that U.S. carriers earn on the foreign mobile surcharges they impose on U.S. consumers. In principle, KDDI does not object to a reasonable mark-up and it normally prefers that the pricing practices of carriers should be governed by marketplace forces rather than regulation. However, if the FCC is concerned that the surcharges imposed by U.S. carriers are imposing an undue burden on U.S. consumers, the FCC should focus on the high profit margins that U.S. carriers are earning on these surcharges rather than exploring the possibility of intervening to affect the level of foreign mobile termination rates.

There is recent FCC precedent for prohibiting U.S. carriers from marking-up costs that they recover from subscribers through surcharges. In a *Report and Order* released two months ago, the FCC held that U.S. telecommunications carriers who pay into the Universal Service Fund ("USF") may not mark-up the specific line-item surcharges that they impose on customers to recover their USF payments. *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket Nos. 96-45, et al., FCC 02-329, rel. Dec. 13, 2002 (Report and Order and Second Further Notice of Proposed Rulemaking), at ¶¶ 45-63. The FCC held that "the practice of marking up federal universal service line-item charges above the relevant assessment amount will be prohibited prospectively." *Id.* at ¶ 49. The FCC adopted this rule because some U.S. carriers were imposing a line-item USF surcharge on certain customers that "significantly" exceeded the relevant USF contribution factor for those customers. *Id.* at ¶ 46. The FCC expressed concern that some U.S. carriers were using USF surcharges to recover costs that were "completely unrelated" to their USF payments. *Id.* at ¶ 47.

In sum, KDDI recommends that the FCC defer to foreign NRAs regarding the regulation of foreign mobile termination rates, and that the FCC instead focus on the surcharge pricing practices of U.S. carriers and ensure that surcharges are cost-based and do not embody excessive profit margins.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that copies of KDDI Corporation's Reply Comments were served this 19th day of February, 2003, by mail, postage prepaid, upon the following:

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